

Valuation Accuracy: A Critical Commentary of Dubai's Real Estate Sector

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Background

Research Rationale

- The issue of valuation accuracy is important for property professionals and investment analysts, particularly given the recognition that real estate has now become a major global asset. Property valuations are a significant driver in investment and broader purchasing decisions, both through market transparency and consumer confidence.
- Values can be difficult to assess due to different concepts of value, its inherent subjectivity and the heterogeneity of property.
- Inaccuracy or 'valuation bias' can be exacerbated with the addition of uninformed local practices or mis-information and lacking transparency (market efficiency)
- In the preliminary stages of this PhD research, the author is seeking to examine the extent of valuation error introduced by not adopting standardized features within its market, including that of property market information
- Recent research including that of Dunse, Jones & White (2010) supports the premise of this research in that "...valuation accuracy is a function of information availability."
- Key observations borne out from this research include that the lack of information flows within Dubai's real estate industry and the high levels of secrecy surrounding the sharing or pooling of market data amongst firms and practitioners. Furthermore, the main provider of real estate information, REIDIN, has been reported as being fundamentally flawed and lacks the credibility of information sources available in more mature markets. The findings of this study have important implications for fund/portfolio managers, investors and real estate valuers concerned with defining market price, volatility & risk.

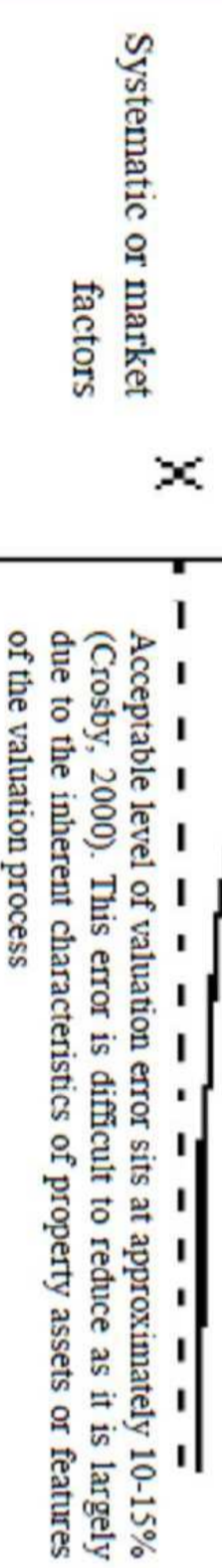
What is Property Value?

Theoretical Observations

- Property valuations have long been considered as a 'subjective' process whereby the knowledge and professional competence of the valuer are key determinants of the mode of accuracy within a valuation or appraisal
- Property valuations are greatly exposed to sources of valuation error; be it through misunderstood definitions of what 'value' is; the influence of client behaviour and bias; inappropriate knowledge and understanding.
- In a broader understanding of valuation accuracy, market observers are in agreement that:
 - All valuations are *opinions*, each holding a varying degree of *subjectivity*
 - Uncertainties affect all properties however different uncertainties are determined by the individual characteristics of a property and its location
 - With the reliance upon the comparable method in property valuations, data availability and information efficiency are paramount to the accuracy of real estate valuations
 - In open and transparent markets one can gauge market value relatively straightforward with comparable evidence. In emerging markets this is more complex
- Figure 1.1 highlights the levels of valuation error that can be removed through a range of non-systematic factors. In essence the presence of such factors develops as the maturity of a country's real estate market also develops. However, there is a certain degree of error (OX in Figure 1.1) that cannot be removed due to the subjectivity of real estate valuations as well as error introduced by the inherent features of property assets characteristics (such as heterogeneity, time lags in market information).

Non-systematic or specific factors

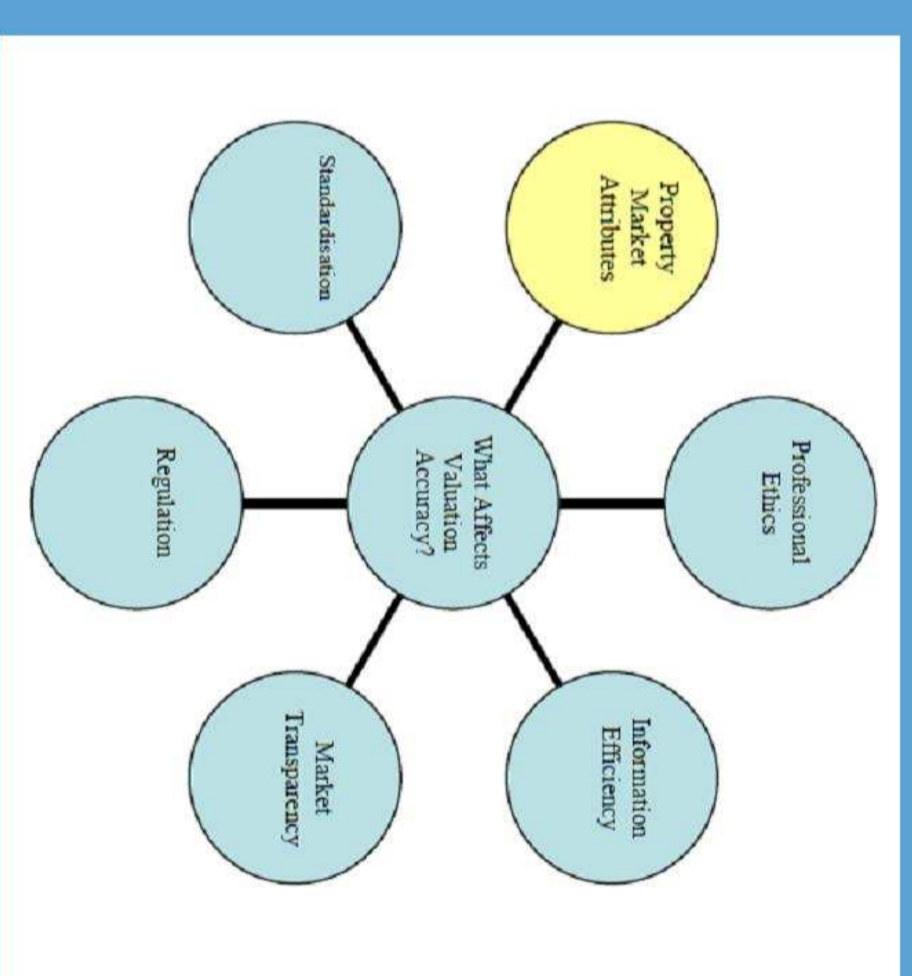
Reduction in valuation error as non-systemic risks are diminished. These would be features of local property markets that create higher levels of valuation error to occur in the marketplace ('standardisation' – see Figure 2)



What Affects Valuation Accuracy?

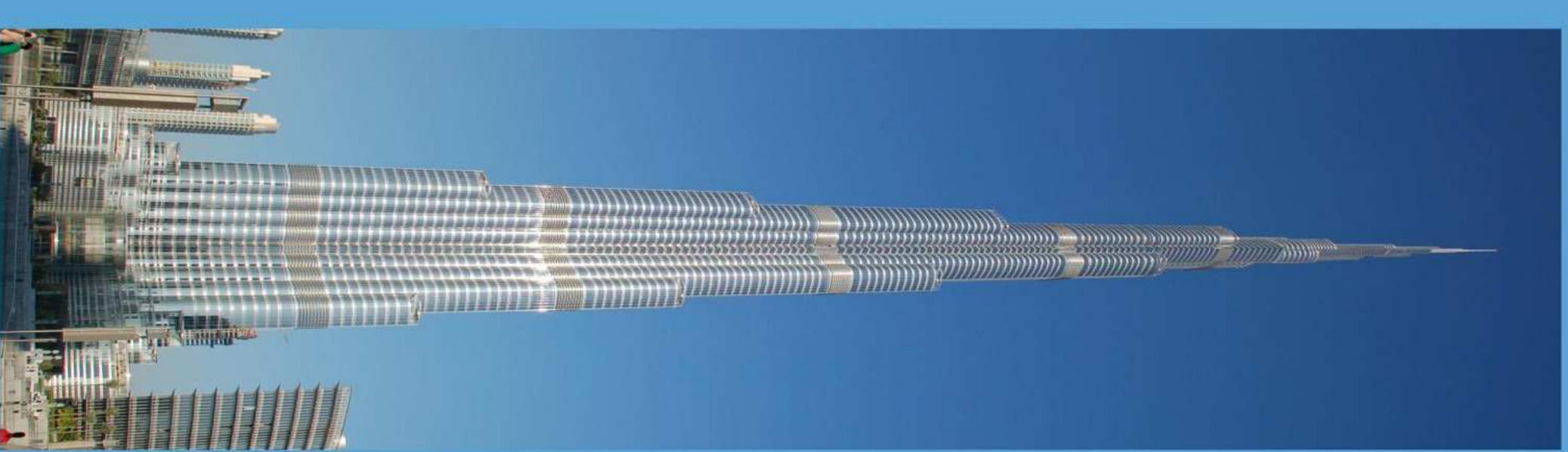
Market Observations

- This paper and subsequent research by the author on this topic will claim that non-market risk for properties "is a higher proportion of total valuation error than in other major asset markets". The latter is also a subject of market maturity for individual countries when looking at global comparisons of valuation error.
- The accuracy of valuations is shown to be somewhat dependant upon local variable factors such as the extent of information, variability of local cycles and the heterogeneity of the stock itself. Figure 1.2 goes on to highlight the broad categories of market practice that affect valuation accuracy in real estate. Those variables shown in 'blue' are examples of non-systematic or specific risk and those in 'yellow' represent systematic error. It is this framework that will be assessed in the context of Dubai's real estate sector



Research Questions

- What are the dominant real estate property market assessment explanatory variables and models revealed through existing research and what success if any, has been achieved in the application of valuation assessment methods and information forecasts?
- On what basis do property professionals and valuers currently apply property market information in the valuations they undertake?
- Does varying information flow and accuracy have a significant impact on the results of asset valuation assessments?
- What is the impact of client influence and ethical behaviour of valuers?
- Will producing more detailed information on various real estate segments (residential, commercial, retail & industrial) and the assets within, on a sub-market or precinct level within Dubai generate improved valuation accuracy?



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